30 September 2013 - Statement by the EC and the ECB following the conclusion of the fourth review of the financial assistance programme for Spain

A delegation from the European Commission, in liaison with the European Central Bank, carried out the fourth review of the financial sector assistance programme for Spain from 16 September to 27 September 2013. The International Monetary Fund also participated in the review, fulfilling its role as an independent monitor. Meetings were also attended by the European Stability Mechanism and the European Banking Authority. On the basis of the review, it can be concluded that the programme remains on track.

Spanish financial markets have further stabilised. Following the drop in sovereign bond yields, financing conditions for large parts of the economy have improved, amidst lower volatility. The liquidity situation and the financing structure of the Spanish banking sector have further improved as bank deposits have been rising and Spanish banks are regaining access to funding markets. The solvency position of Spanish banks has remained comfortable after the recapitalisation of parts of the banking sector, the transfer of assets to SAREB (the Spanish asset management company) and overall positive earnings results of Spanish banks over 2013 so far.

The process of restructuring of banks having received State aid is well underway, guided by the restructuring plans as adopted by the European Commission. The foreseen burden-sharing exercises with banks´ shareholders and junior bond holders are virtually completed.

Compliance with the horizontal policy requirements in the Memorandum of Understanding is nearly complete, and, thereby, the governance, regulatory and supervisory framework of the Spanish banking sector has been strengthened, which translates into higher shock resilience of the banking sector going forward. Efforts to adopt the agreed measures and their implementation need to continue as envisaged, in particular in the area of the reform of the governance of the savings banks. Steps have already been taken aiming at improving non-banking financial intermediation.

Nevertheless, the broader economic environment has continued to weigh on the banking sector. Lending to the economy is still contracting substantially, in particular against the backdrop of weak demand for new lending and persisting EU banking markets' fragmentation. While there are early signs of a general economic stabilisation, both the private and public sector need to reduce their debt stocks going forward, and the adjustment in the real estate market is still ongoing. Both elements still impinge on the profitability prospects of banks, even if the bulk of the effect of real estate assets deterioration on banks' profitability has already been accounted for through special provisioning. Therefore, supervisors and policy makers have to continue to monitor decisively the process of stabilising the banking sector. Sustained proper diagnostics of the shock resilience and solvency of the Spanish banking sector remains vital. Efforts to increase transparency of the balance sheets of Spanish banks are important, and therefore the recent initiatives to harmonise treatment of refinanced and restructured loans are welcome. Also, the current development of a forward-looking exercise of the banking sector by the Banco de España appears as a useful supervisory tool.

The economy is showing signs of bottoming out, supported in particular by net exports. Going forward, the central scenario remains one of a mild recovery in activity, as the ongoing correction of external and internal

imbalances and high unemployment put a lid on output growth. Visible advances in the reform agenda have contributed to the recovery in confidence in the Spanish economy in recent months. It is crucial that the positive reform momentum is maintained, so as to ensure the rapid completion of legislative and implementation processes underway. These include reforms to stabilise the pensions system, unify the Spanish internal market, liberalise professional services, deliver more effective local and public administration and make product and services markets more dynamic. These reforms will support the adjustment process and competitiveness and contribute to underpin durably fiscal consolidation, which remains essential to stem and reverse the rise in general government debt. Meeting the agreed deficit reduction path is essential to reverse the rise in general government debt and consolidate the improvement in market confidence.

The next review is foreseen to take place in December 2013.